

Digest of a Performance Audit of Public Utility Regulation in Utah

The development of partial competition in the telecommunications, electric power and natural gas industries is requiring the state to reevaluate its approach to public utility regulation. The current organizational structure and regulatory practices were designed to support the regulation of monopoly providers in which the focus was on setting utility rates and making sure services were adequate and reliable. The development of competition will bring significant changes to some segments of the utility industries that will require corresponding changes in the way the state regulates those industries. The process of addressing these changes will require the participation of both the Legislature and state regulatory staff.

Historically, the public utility industries have operated as government regulated monopolies. In exchange for the right to be the exclusive provider for a service region, utility providers agreed to submit to government regulation. In addition to monitoring service quality, a primary task of regulators has been to examine the prudence of utility expenditures and establish rates that allowed a utility provider the opportunity to earn a fair return on investment. Because disputes over utility rates are generally resolved through trial-like proceedings, the state has adopted an organizational structure designed to facilitate the judicial role of the Public Service Commission. In order to protect the commissioners from unfair influence or “*ex-parte*” communication with those who argue cases before them, state policy makers decided that the technical staff could not work directly for the commission. A separate agency, the Division of Public Utilities, houses the regulatory staff who actually monitor utility activities and advocate actions before the commission. Commissioners have a small staff of advisors to help them interpret the information presented during proceedings and to help them write orders and establish rules. Both the commission and division represent the broad public interest. A third agency, the Committee of Consumer Services, has a small staff who represent the interests of the residential and small business consumers during commission proceedings.

Changes in utility industries are leading to changes in their regulation. In 1995, the Utah Legislature passed a telecommunications reform act that has paved the way for the restructuring of that industry. The Legislators may soon consider similar reforms for the electric power industry and perhaps some day for natural gas industry. For their part, state regulatory staffs are using more informal procedures to address the policy issues associated with a partially competitive, partially monopolistic marketplace. Although the state will need to continue to rely on traditional regulatory tools to regulate those segments of the market that remain uncompetitive, regulators are now placing an increased emphasis on the development of the new rules, policies and procedures to govern competitive segments of the marketplace.

This report discusses the challenges of regulating industries that are partially competitive and partially monopolistic. Our work included a review of how other states are responding to similar challenges. In many ways, Utah’s regulators are making similar changes as other states. However, Utah’s favorable conditions of relatively low utility rates and financially healthy providers make changes less urgent here than in some states. The following summarizes the

major conclusions in this report:

Quasi-legislative Techniques can be Used to Resolve Policy Issues. As competition develops in the public utility industries, state utility regulators are devoting an increasing amount of their time to developing the new rules, policies and procedures for the future marketplace. Historically, most states relied on adjudicative proceedings to resolve many issues. Increasingly, however, states are relying on “quasi-legislative” techniques to make decisions that have industry-wide applicability. Although Utah has been using many of the informal policy-setting procedures, there are a number of forces that are encouraging the commission to resolve industry-wide policy issues during adjudicative proceedings. We feel state regulators’ use of quasi-legislative procedures to address industry-wide policy issues is appropriate and encourage utilities, consumer interests, potential new competitors, and the Legislature to support this process.

Legislature Should Provide Broad Guidance. It is the Legislature that decides whether to reform state regulation of an industry and establishes the objectives of the reform process. In telecommunications, the Legislature has already provided important guidance by approving the Utah Telecommunications Reform Act of 1995. Legislators may soon need to provide similar guidance on possible reform of the electric power industry. Based on our observations of other states, we provide legislators with a number of specific suggestions for how they can provide regulators with the broad guidance they need. These include: (1) providing legislation containing broad language on competitive expectations or offering specific “guiding principles” for restructuring efforts, (2) setting deadlines for achieving certain milestones in the reform process, (3) outlining a process that regulators should use as they develop market forms, and (4) creating a legislative committee that can act as a focal point for legislative consideration of utility issues. However, while the Legislature should offer broad guidance, we feel that legislators should rely on the technical expertise of state regulatory staff for detailed decision-making.

Organizational Structure Should be Examined. Legislators asked us to review the roles of the commission, division, and committee and to determine if the three agencies can be consolidated. One option is to consolidate the commission and the division, as they are in most other states. While consolidation should be considered, there are advantages in keeping the organizational separation. Moreover, the fact that utility regulators are engaged in a difficult market reform process may make this a poor time for a major organizational change. As an alternative to taking immediate action, we feel legislators should consider initiating a strategic planning process to evaluate possible organizational changes in the context of a broad reform of public utility regulation in Utah, including future statutory, policy, and staffing needs. In addition, we feel the Legislature should clarify the organizational independence of the Committee of Consumer Services.